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## SERA Policy Brief

### *The Business Environment and Incentives for Tanzanian Agriculture<sup>1</sup>*

Tanzania has had difficulty attracting large foreign investors into the agriculture sector because of the lengthy and uncertain procedures for acquiring land, high corporate and local taxes, and high operating costs. Incentives available to foreign investors are not sufficient to offset these constraints. Restrictions on the occupation of land by majority-owned foreign companies, while intended to prevent land speculation, may discourage legitimate foreign investors. In contrast, the business environment and incentives in Mozambique and Zambia are more favourable for foreign investors. Procedures for acquiring land in Mozambique are similar to those in Tanzania, and they have also made it difficult for Mozambique to attract foreign investors; while land use rights can be purchased without government approval in Zambia and that has helped Zambia to attract a large number of foreign-owned enterprises to the sector. If Tanzania is to attract large foreign investors to the agricultural sector; it will need to make land more easily available, provide more favourable incentives, reduce corporate and local taxes, and reduce restrictions on occupation of land by majority-owned foreign companies. A better alternative might be to concentrate on attracting medium-sized domestic investors to the sector as has been done in Mozambique.

Agriculture accounts for about three-quarters of employment in Tanzania and increasing the number of large agricultural enterprises would increase wage employment in the sector and provide more opportunities for outgrowers. Employment is one of the main benefits of attracting large agricultural enterprises, but these enterprises can also expand the tax base, provide produce for the domestic market, contribute to export earnings, and support services to local communities such as schools and clinics. They can also bring needed capital, technology, management skills, and marketing linkages. Attracting foreign investors to develop large

<sup>1</sup> This Policy Brief was prepared by Don Mitchell and Edith Lazaro, Senior Advisor and Research Associate of the SERA Project, respectively, in collaboration with Daktari Hango from the Ministry of Agriculture, Livestock and Fisheries, James Ngwira of the President's Delivery Bureau, Emmanuel Lyimo of the SAGCOT Centre, and Martin Masalu of the Tanzania Investment Centre. The SERA Policy Project is a USAID-funded Feed the Future Project that seeks to improve agricultural policies in Tanzania and build capacity for policy analysis and advocacy. It is implemented by Booz Allen Hamilton.

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agricultural enterprises has been the cornerstone of Kilimo Kwanza, SAGCOT, and Big Results Now; but Tanzania has not been successful in attracting large foreign investors largely due to the poor business environment. The SERA Policy Project of the USAID Feed the Future Initiative in collaboration with the Ministry of Agriculture, Livestock and Fisheries (MALF), the President's Delivery Bureau (PDB) for Big Results Now (BRN), the Southern Agricultural Growth Corridor (SAGCOT) Centre, and the Tanzanian Investment Centre (TIC) undertook a study of the agricultural business environment and incentives and compared them with the business environment in Mozambique and Zambia. The study found a wide range of outcomes, with Zambia having more than 1,000 large commercial farms while Tanzania has struggled to attract even a few. Mozambique has been more successful than Tanzania at attracting foreign investors, but trails Zambia by a wide margin. A comparison of the business environment and investment incentives showed some similarities between the three countries but also large and important differences. Access to land and the ability of an investor to capture land value appreciation emerged as important factors in attracting foreign investors, while other aspects of the business environment and incentives were more important to operating profitability and sustainability. This Policy Brief compares these countries with respect to corporate and local taxes, the cost of selected inputs, availability and access to land, agricultural and land policies, and incentives.

## Comparing Tanzania, Mozambique, and Zambia

The three countries are similar in many respects, with all dependent on agriculture for a large share of employment and all having a large smallholder sector with average land holdings of less than two hectares. All three countries have had rapid GDP growth over the past decade, but Tanzania has had slower growth than Mozambique or Zambia by about one percentage point in GDP and per capita GDP (Table 1). Per capita GDP varied from USD586 in Mozambique to USD955 in Tanzania and USD1,722 in Zambia. The share of agriculture in GDP varied from a high of 31.5% in Tanzania to a low of 18.0% in Zambia.

**Table 1: Country Comparisons.**

	----- Tanzania -----	---- Mozambique----	----- Zambia-----
<i>GDP Growth Rate 2005-14 (%)</i>	6.6	7.5	7.7
<i>Population Growth Rate</i>	3.2	2.8	3.1
<i>Per Capita GDP Growth Rate 2005-14 (%)</i>	3.3	4.5	4.5
<i>Per Capita GDP (USD) 2014</i>	955	586	1,722
<i>Agr. Share of Employment (%)</i>	75	75-80	80
<i>Agr. Share of GDP 2014 (%)</i>	31.5	25.2	18.0

**Sources:** World Bank, Tanzania NBS, Instituto Nacional de Statistica Mozambique, Central Statistics Office, Zambia.

## Access to Land and the Potential to Benefit from Land Value Appreciation

Tanzania has an estimated 44.0 million hectares of arable land suitable for crop production, and only one-quarter of that is cultivated. Mozambique and Zambia also have large areas of arable land suitable for crops that are not being cultivated and together these three countries account for one-half of the arable land in Sub-Saharan Africa that is uncultivated, with high agricultural potential, and low population density. <sup>i</sup>However, uncultivated does not mean unclaimed, and most of the land is under community control and cannot be easily

<sup>i</sup> World Bank (2011), *Rising Global Interest in Farmland*, page xxxiv.

or quickly accessed by investors. As arable land becomes scarcer in other regions, investors will increasingly turn to Tanzania for cropland. This interest is driven partly by the potential for land price increases which are an important part of the total return to investments in agriculture. In the U.S., for example, net cash income (cash income minus cash expenses) provided an average return on assets of 5.2% per year from 2000 to 2015 while increases in land values accounted for an additional 5.5% of returns per year.<sup>ii</sup>

The ability of a foreign investor to benefit from land value appreciation in Tanzania is limited because the Land Act (1999) restricts the rights of majority-owned foreign companies and specifies that the land rights revert to the Tanzania Investment Centre or other authority prescribed by the Ministry at the expiry, termination, or extinction of the right of occupancy or derivative right.<sup>iii</sup> How this provision would be applied is not clear, but it may limit an investor's opportunity to benefit from the appreciation in land values. The Land Act further states that unexhausted improvements may be compensated under this Act but the mechanism is not described. While the intent of the restriction on majority-owned foreign companies is to discourage land speculation, it also discourages legitimate investors. By comparison, Zambia has an active land market that allows investors to acquire and sell land quickly. Since land use rights can be sold in Zambia, an investor can capitalize on its increase in value. This has helped to attract a large number of commercial farms, especially from neighbouring Zimbabwe and South Africa. There are about 1,000 commercial farms with 1,000 hectares or more and about 10 with more than 40,000 hectares.<sup>iv</sup> Without the potential to benefit from land value appreciation and the capture of the value of improvements made to the land, the business environment becomes much more important in attracting large commercial agricultural enterprises.

## Corporate Income Taxes

Corporate income taxes are an important part of the business environment, and Tanzania applies the standard corporate income tax rate of 30% to agricultural processing and production (Table 1). In contrast, Mozambique applies a reduced rate of 10% on farming and cattle breeding, and Zambia applies a 10% corporate tax rate on agricultural production and processing (field and factory operations). The implications of the different corporate income tax rates on profitability can be shown with an example of a hypothetical sugar company operating in each of the three countries.<sup>v</sup> Profits for the identical sugar company in Tanzania are 78% of those in Zambia and 89% of those in Mozambique just due to the differences in corporate tax rates. However, corporate tax rates are only one of the many differences in taxes and expenses encountered by a corporate investor in Tanzania.

**Table 2: Corporate Income Tax Rates.**

	----- Tanzania -----	---- Mozambique----	----- Zambia-----
<i>Standard Rate (%)</i>	30	32	35
<i>Agro-Processing (%)</i>	30	32	10
<i>Agr. Production (%)</i>	30	10	10

**Source:** KPMG, PWC

<sup>ii</sup> Net Cash Income is from USDA/ERS Farm Income and Wealth Statistics.

<sup>iii</sup> Land Act (1999). Page 26, para 20, section (5)

<sup>iv</sup> The uncertainty of land security in Zimbabwe also encouraged many farmers to migrate to Zambia.

<sup>v</sup> Field and factory costs are about equal in a typical sugar company and are set equal in this example. The differences in profits then depends only on the corporate tax rate on field and factory operations.

## Local Taxes

Local Government Authorities (LGAs) in Tanzania are allowed to collect taxes by the Local Government Finance Act (1982), and the largest of these taxes is the crop produce cess which accounts for 43% of rural LGA's revenues.<sup>vi</sup> The crop produce cess is a tax on the gross value of production, and it is primarily directed at traditional export crops but also affects food crops. The crop produce cess varies by district and is typically levied when crop produce is moved from one district to another. Corporate producers are more visible than smallholders and it is more difficult for them to avoid the tax, although some have been able to negotiate reduced rates. The tax rate was capped at 5% by the central government in 2003. By comparison, Mozambique does not have a crop produce cess and Zambia has one at the rate of .03%. Since the crop produce cess is a tax on production, it can have a very large impact on corporate profits especially when profits are low. In addition to the crop produce cess, there are many other local taxes and fees in Tanzania and they include: OSHA, Fire, Business License, Billboard Fee, Environmental Fee, Waste Management Fee, Business Registration and License Fee, Workers' Check-up Fee, Weights and Measures Levy, and Fuel Levy. There is also a Service Levy of 0.03% of gross turnover collected by local communities. Unfortunately, the study team was not able to obtain a comparable list of local taxes in Mozambique and Zambia.

## Other Taxes and Operating Expenses

In addition to high corporate and local taxes, the Value Added Tax in Tanzania is 18%, compared to 17% in Mozambique, and 16% in Zambia. Lending interest rates are 16.3% in Tanzania, compared to 14.3% in Mozambique, and 11.6% in Zambia. Electricity rates are 16.7 U.S. cents per kilowatt hour in Tanzania compared to 7.0 in Mozambique, and 4.8 in Zambia. Other taxes and fees include workers' compensation (1% of wages), skills development levy (5% of non-farm wages), and corporate contribution to the National Social Security Fund of 10% of wages compared to 5% in Mozambique and 4% in Zambia. The combined effects of these taxes and fees is to further reduce profitability of corporate enterprises in Tanzania compared to Mozambique and Zambia.

**Table 3: Other Taxes, Fees and Expenses.**

	----- Tanzania -----	---- Mozambique----	----- Zambia-----
VAT (%)	18.0	17.0	16.0
Interest Rates (%)	16.3	14.3	11.6
Electricity (U.S. cents/kwh)	16.7	7.0	4.8
National Social Security Fund (% of wages)	10.0	4.0	5.0
Skills Development Levy (% of non-farm wages)	5.0	0.0	0.0

**Source:** KPMG, PWC, World Bank, Various Country Statistical Reports. Lending interest rate <http://data.worldbank.org/indicator/FR.INR.LEND>

<sup>vi</sup> The United Republic of Tanzania, "Agricultural Produce Cess in Tanzania: Policy Options for Fiscal Reforms"



## Agricultural Policies

Agricultural policies and their implementation are an important component of the business environment and frequent changes or ad hoc government interventions increase risk for investors and discourage investment. For example, the Government of the United Republic of Tanzania (GoT) recently announced a cap on sugar prices and threatened to prosecute companies found to be withholding sugar from the market in an effort to increase prices.<sup>vii</sup> Such interventions are rarely effective, but signal to investors that government is ready to intervene rather than rely on market forces to solve problems.

The agricultural policies of Tanzania, Mozambique, and Zambia are similar in their basic approach. All three countries protect selected sub-sectors with tariffs and quantitative controls. Marketing in all three countries is primarily done by the private sector, with the exception of staple food crops which are primarily produced by smallholders. Tanzania and Zambia have large input subsidy programs for smallholders while Mozambique does not. Tanzania and Zambia have a national food reserve which also serve a dual role of holding large food reserves and intervening in markets to influence prices. Policy coherence and stability are a challenge in all countries.

Trade policies are similar in all three countries, with all countries relying on export and import permits, tariffs, and quantitative controls to protect sensitive crops. In Tanzania, rice and sugar have high tariffs and permits are required for imports. Marketing in all three countries is largely done by the private sector, with the exception of maize which has varying degrees of government marketing involvement.

## Investment Facilitation and Incentives

Tanzania, Mozambique, and Zambia all have one-stop investment centres to assist investors to establish their business and identify investment opportunities. Tanzania has the Tanzania Investment Centre (TIC) which is an agency of the Ministry of Industries, Trade, and Investments; Mozambique has the Centro de Promoção de Investimentos (Investment Promotion Centre) which is under the authority of the Ministry of Economy and Finance; and Zambia has the Zambia Development Agency which is a semi-autonomous institution under the authority of the Minister of Commerce, Trade, and Industry. Mozambique also has an Agricultural Promotion Centre (CEPAGRI) which is a government institution under the authority of the Ministry of Agriculture to assist investors in agriculture. All provide incentives to investors, and special incentives to strategic investors of a certain size.

In Tanzania, a local investor must invest at least USD100,000 and a foreign investor must invest at least USD500,000 to qualify for the certificate of investment incentives. To qualify as a Strategic Investor, which allows additional incentives, a local investor must invest at least USD20 million and a foreign or joint venture investor must invest at least USD50 million. A Super Strategic Investor must invest at least USD300 million and can negotiate a special package of incentives. In Zambia, the largest category of investor is a Major Investor who must invest at least USD10 million and can negotiate the package of incentives.<sup>viii</sup> In Mozambique, an investor who invests about USD88,000 (depending on the exchange rate) is eligible for general investment incentives and a Large Scale Investor who invests at least USD500 million or an investor in a priority sector receives additional investment incentives.<sup>ix</sup>

<sup>vii</sup> Draft Report, October 2014.

<sup>viii</sup> The Citizen, "Govt order on sugar price flops" Thursday, 10 March 2016.

<sup>ix</sup> Zambia Development Agency: Investor Guide Book February 2013.  
Mozambique Investment Guide, February 2013.

## Conclusions and Recommendations

Tanzania, Mozambique, and Zambia are land abundant countries which together account for one-half of the high-potential, underutilized crop land in Sub-Saharan Africa. This has led to a surge of investor interest in establishing agricultural enterprises, and attracting such large agricultural enterprises has been the cornerstone of Tanzania's Kilimo Kwanza, SAGCOT, and Big Results Now Initiatives. However, Tanzania has not been successful in attracting such enterprises despite government efforts and initiatives such as SAGCOT. In contrast, Zambia has been very successful in attracting such large-scale agricultural enterprises and Zambia has more than 1,000 farms with 1,000 hectares or more and 10 farms with more than 40,000 hectares. The largest, ZAM-BEEF, has more than 80,000 hectares of land and is listed as a share company on the national stock exchange. Mozambique has not been able to attract the mega-farms like Zambia, but it has been able to attract medium-sized domestically-owned farms into the sector while Tanzania has not been successful in attracting either. The agricultural business environment largely explains the differences with Zambia providing favourable incentives, an attractive business environment, easy access to land, and an active land market where an investor can sell their land rights. Mozambique has provided favourable incentives and an attractive business environment, but not easy access to land and makes the sale of land rights illegal. Tanzania provides neither favourable incentives nor a favourable business environment, and does not provide easy access to land. It also restricts the rights of majority foreign-owned enterprises to transfer land rights. If Tanzania is to attract large- or medium-scale agricultural enterprises, it will need to make land more easily available to investors, improve the business environment, and provide greater incentives to the sector.

Access to land seems to be the most important factor determining where an international investor will locate within the region. Zambia has large tracts of land titled to individuals that can be leased to investors on a short- or long-term basis and sold or leased to another investor without government approval. That makes it possible for an investor to acquire land quickly if they are prepared to pay market prices. There is an active land market in Zambia which allows an investor to benefit from the appreciation of land values when they sell their lease, and the appreciation of land values is an important part of the total return to agriculture. Mozambique does not provide easy access to land and even makes it illegal to sell land. Land titles cannot be sold or transferred and revert back to the government upon termination of the lease, and a new investor is required to apply for a new title from the Ministry of Land. That effectively prevents an investor from selling their title and benefiting from land value appreciation or improvements made to the land. Acquiring land by an investor in Tanzania is also difficult and the title reverts to the government upon expiration or termination which limits an investor's ability to transfer the title to another investor and benefit from the appreciation of land values. Without the ability to transfer the land lease, an investor cannot sell their investment and that discourages investment, especially by foreign investors.

The agricultural business environment is also an important determinant of where an international investor might choose to locate in the region and is critical to the profitability and sustainability of an agricultural enterprise. Tanzania has the least favourable business environment of the three countries studied because of high taxes and high operating costs. The standard corporate income tax in Tanzania is applied to all corporations while Mozambique and Zambia offer preferential rates to agricultural investors. Tanzania also has numerous local taxes and fees, including the crop produce cess which is a tax of up to 5% on the gross value of crop

production, while Mozambique and Zambia have fewer and small local taxes and fees. The crop produce cess in Tanzania is especially burdensome when profits are low as is often the case. Other taxes and operating expenses are also higher in Tanzania, with the VAT at 18% in Tanzania, compared to 17% in Mozambique, and 16% in Zambia. Interest rates, electricity rates, and corporate contributions to pensions are also higher in Tanzania than in the other countries. These various factors combine to create an unfavourable business environment for agricultural producers in Tanzania compared to Mozambique and Zambia.

Large agricultural enterprises can make valuable contributions to agricultural development and the government has shown its commitment to attract foreign investors. However, Tanzania is not competitive at attracting large foreign investors into the agricultural sector. If Tanzania wants to attract large foreign investors, it will need to make land more easily available, reduce corporate taxes, reduce or eliminate the crop produce cess, and improve other aspects of the business environment. Current land laws prevent a foreign investor from recouping investments made to the land or benefiting from land value appreciation which removes one of the main sources of returns to agricultural investors. The process for acquiring land is also long and uncertain and most investors would not have the financial resources or persistence to acquire land from either the central government or local communities. Opportunities to attract medium-sized domestic investors into the sector are greater than attracting large foreign investors and that is the approach being taken in the Beira Corridor in Mozambique. These investors can more easily acquire land and are more familiar with the business environment. A similar approach should be considered by SAGCOT, and additional incentives might be provided such as reduced corporate income taxes and VAT exemptions.

## References and End Notes:

- (i) World Bank (2011), Rising Global Interest in Farmland, page xxxiv.
- (ii) Net Cash Income is from USDA/ERS Farm Income and Wealth Statistics.
- (iii) Land Act (1999). Page 26, para 20, section (5).
- (iv) The uncertainty of land security in Zimbabwe also encouraged many farmers to migrate to Zambia.
- (v) Field and factory costs are about equal in a typical sugar company and are set equal in this example. The differences in profits then depends only on the corporate tax rate on field and factory operations.
- (vi) The United Republic of Tanzania, "Agricultural Produce Cess in Tanzania: Policy Options for Fiscal Reforms" (vii) Draft Report, October 2014.
- (viii) The Citizen, "Govt order on sugar price flops" Thursday, 10 March 2016.
- (ix) Zambia Development Agency: Investor Guide Book February 2013.  
Mozambique Investment Guide, February 2013.